

## DISCUSSION CALENDAR

### Agenda Item # 6

## AGENDA REPORT SUMMARY

**Meeting Date:** March 23, 2021

**Subject:** Resolution No. 2021-##: Approving Fiscal-year 2020-21 Mid-year Financial Update, budget adjustments, and updated Salary Schedule

**Prepared by:** Richard Martinez, Finance Consultant

**Reviewed by:** Jon Maginot, Interim Administrative Services Director

**Approved by:** Brad Kilger, Interim City Manager

**Attachment(s):**

1. Resolution No. 2021-##
2. Updated Salary Schedule

**Initiated by:**

Staff

**Previous Council Consideration:**

N/A

**Fiscal Impact:**

The proposed budget amendments for the Operating Budget total a reduction of \$2.75 million in General Fund revenues and a reduction of \$1.45 million in General Fund Expenditures. In addition, the proposed adjustments include the assignment of \$7.8 million in unassigned fund balances.

**Environmental Review:**

Not applicable

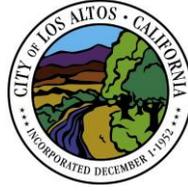
**Policy Question(s) for Council Consideration:**

- Does the Council concur with the Mid-year Financial Update and budget adjustments?

**Summary:**

- Property tax revenues continue to be strong, however they are trending slightly under the amount budgeted. All other revenues, with the exception Community Development and Police fees, continue to struggle as a result of the current economic conditions. Expenses City-wide are under budget at the mid-year point.
- Only minor adjustments are recommended to the Operating Budget at this time. These adjustments total \$100,000 and are discussed later in this report.
- \$7.8M in fund balance from FY 2019-20 is being added to our reserves. The recommended appropriation to the Operating Reserve and CIP fund is also highlighted.

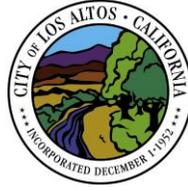
**Staff Recommendation:**



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Adopt Resolution No. 2021-##, approving the Fiscal-year 2020-21 Mid-year Financial Update, budget adjustments, and updated Salary Schedule, including assignment of fund balance as outlined



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### **Purpose**

To review revenues and expenses for the first half of FY 2020-21 in comparison to the Adopted FY 2020-21-1 Budget and to make adjustments, if necessary. The mid-year review is also when the Council assigns fund balance when applicable and reviews its reserves.

### **Background**

The City Council-approved Operating Budget serves as the annual plan and resource allocation that guides and ensures implementation of City Council policies and priorities. The budget implements the vision and direction for the range of services that meet the needs of the community.

The financial review, as of December 31, 2020, provides the mid-year budget update to the City Council for the current fiscal year. Analysis of the revenues collected and all expenditures through December 31, 2020 measures the budget's adherence to the established resource allocation plan. Proposed budget amendments make the necessary adjustments identified during the mid-year financial review.

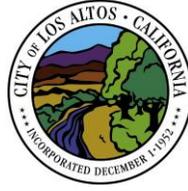
### **Discussion/Analysis**

City finances, as expected have been negatively affected by the economic downturn at the mid-year point of the City budget. Hardest hit of the revenues are the Transient Occupancy Tax and Recreation Fees, followed by Utility User Tax. On the bright side, property tax continues to show solid growth and Sales Tax is holding steady and is expected to meet or slightly exceed budget. Property Tax and Sales tax tend to always be below the 50% mark at mid-year due to timing delays in when the City receives the tax dollars. City expenditures demonstrate prudent fiscal management as departments are operating within their allocated budget amounts and in most cases below the 50% mark at mid-year.

### **General Fund**

The FY 2020-21 General Fund budget was approved on June 23, 2020 for \$44.9 million in revenues with expenditures and debt service transfers out of \$43.6. The approved budget had planned for a surplus of approximately \$1.3 million. Even though revenue estimates were lowered at the time due to the current economic conditions, it appears at the 50% juncture they will come in even lower. While it is difficult to precisely estimate what the final revenues will be, due to uncertainties as to when things will resume to normal, a rough estimate at this time is that General Fund revenues will be \$2.8M lower than budgeted.

As mentioned, the FY 2020-21 General Fund expenditures and debt service transfers out were approved for \$43.6 million. As of December 31, 2020, expenditures were at 43% of budget (44% last year), below the expected 50% level. A more detailed breakdown of revenues and expenses is outlined below:



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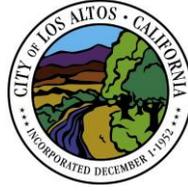
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**General Fund Revenue**

General Fund Revenues	Approved FY 19/20 Budget	YTD Actual FY 19/20	Approved FY 20/21 Budget	YTD Actual as of 12/31/20	FY 20/21 Budget to Actual %	FY 19/20 Budget to Actual %
Property Tax	25,639,810	25,786,599	27,687,029	8,899,601	32%	101%
Sales Tax	3,301,400	3,373,391	2,641,120	1,002,068	38%	102%
Utility Users Tax	2,781,000	2,838,664	2,864,430	1,118,793	39%	102%
Motor VLF	-	24,686	-	-	0%	0%
Transient Occupancy Tax	3,360,000	2,359,762	1,882,200	220,364	12%	70%
Business License Tax	510,000	517,818	468,180	81,804	17%	102%
Construction Tax	190,600	115,994	190,600	67,508	35%	61%
Documentary Transfer Tax	540,350	579,948	551,157	399,439	72%	107%
Interest Income	362,900	1,770,568	381,045	394,606	104%	488%
Rental Income	24,000	24,106	24,000	-	0%	100%
Recreation Fees	1,477,000	846,586	738,500	21,120	3%	57%
Community Development Fees	3,623,600	3,383,733	3,261,240	1,863,191	57%	93%
Franchise Fees	2,284,540	2,286,957	2,353,076	662,327	28%	100%
Administrative Fees	918,500	1,148,700	918,500	-	0%	125%
Police Fees	329,690	386,390	815,066	444,514	55%	117%
Miscellaneous Revenue	131,226	129,944	131,126	53,753	41%	99%
<b>Total General Fund Revenue</b>	<b>45,474,616</b>	<b>45,573,846</b>	<b>44,907,270</b>	<b>15,229,090</b>	<b>34%</b>	<b>100%</b>

Revenue items of note are:

- The FY 2020-21 actual property tax revenues collected are \$479,000 higher than the prior year as of the mid-year point. As per the latest FY 20-21 Assessed Valuation figures from the County, property values in the City have increased 6.9%. While it is projected that total property tax revenues will exceed prior year's amount by \$1.4 million, it is possible that the final year end revenues will come in under the budgeted amount by approximately \$400,000.
- Sales tax revenues continue to remain steady and are expected to exceed the current year budget estimate, providing that the current economic conditions remain the same or improve but not get any worse. UUT revenues are also expected to come in under budget at year-end by approximately \$400,000, however staff continues to monitor this category closely.
- Transient Occupancy Tax revenues, as mentioned before, is the hardest hit of all the General Fund revenues. If current restrictions continue for the remainder of the fiscal year, the projected year end revenues are expected to be approximately \$1.3 million short of the budgeted amount. This could all change, however, if current restrictions are eased and the economy improves during the last quarter of the fiscal year. TOT revenues as of the mid-year mark represent roughly 5 months of receipts due to the timing delays in the receipt of revenues.



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- Recreation fees are another General Fund revenue source that has been hardest hit due to the COVID-19 restrictions. At the mid-year point, revenues are at a mere 3% of budget and will most likely come in approximately \$700,000 under budget.
- Community Development fees and revenues continue to trend a little higher (57% at mid-year) than expected due to robust construction and various projects throughout the City.

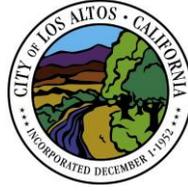
### General Fund Expenditures

General Fund	Approved FY 19/20 Budget	YTD Actual FY 19/20	Approved FY 20/21 Budget	YTD Actual as of 12/31/20	FY 20/21 Budget to Actual %	FY 19/20 Budget to Actual %
<b>Expenditures</b>						
Legislative	\$ 318,017	\$ 369,547	\$ 298,684	\$ 115,801	39%	116%
Executive	3,134,408	4,122,654	3,746,394	2,108,118	56%	132%
Administrative Services	3,971,672	4,022,857	3,546,622	1,467,301	41%	101%
Public Safety	19,615,686	18,795,499	20,593,895	8,471,891	41%	96%
Community Development	3,840,000	3,157,421	3,638,580	1,758,130	48%	82%
Recreation and Community Services	2,696,978	2,313,249	2,545,024	812,736	32%	86%
Public Works	8,898,803	7,832,967	8,564,196	3,901,492	46%	88%
<b>Total General Fund Expenditures</b>	<b>\$ 42,475,564</b>	<b>\$ 40,614,195</b>	<b>\$ 42,933,395</b>	<b>\$ 18,635,469</b>	<b>43%</b>	<b>96%</b>

- For the most part, all departments are currently spending within or below their approved budgets and trending as expected at the mid-year point. Total General Fund Expenditures are at 43% of the annual budget for FY 2020-21.
- The Executive Department is at 56% of budget for the year due additional litigation and election costs incurred in the first half of the fiscal year.

### General Fund Summary

The FY 2020-21 Mid-Year review is one piece in the overall effort of providing sound financial management. It is an integral part in accomplishing fiscal sustainability and it also promotes a transparent and open government. As pointed out earlier, the City began the budget year with the anticipation of having a surplus of \$1.3 million at year end. Given that several revenue sources are projected to come in substantially below budget, that surplus will be eliminated. The total for property tax, UUT, TOT and Recreation fees alone are \$2.8 million. In other words, the City could be facing a \$1.5 million deficit for FY 20-21 if all departments expended their entire allotted budget. It is possible that some General Fund revenues could come in higher, and departmental expenditures could come in under budget. Not to mention the possibility of reductions in COVID-19 restrictions which would positively impact revenues in the last quarter of the fiscal year. With the upcoming preparation of the



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FY 21-22 & 22-23 budget, further scrutiny of current year revenues and expenditures will shed additional light on this. It is worth noting that on March 11, 2021 President Biden signed into law, the American Rescue Plan Act. The relief effort will provide billions in aid to state and local governments and is designed to assist with the budget gaps created by the crisis and its economic shutdowns. Funds the City of Los Altos may receive from this Act are not being considered as part of the mid-year budget review, but, assuming the City receives additional information regarding these funds, will be included in the two-year budget cycle.

**Other Funds**

The Sewer Fund revenues typically lag at mid-year and are at 2% of budget due to timing while expenditures are at 51% of budget.

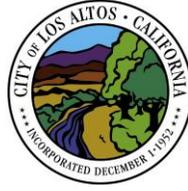
Enterprise Funds	Adopted FY 19/20 Budget	YTD Actual FY 19/20	FY 19/20 Budget to Actual %	Adopted FY 20/21 Budget	YTD Actual as of 12/31/20	FY 20/21 Budget to Actual %
Sewer Revenues	6,483,183	8,321,808	128%	6,483,183	140,320	2%
Sewer Maintenance	7,875,379	5,527,276	70%	5,513,696	2,788,722	51%
Solid Waste Revenues	828,223	1,046,132	126%	852,653	334,442	39%
Solid Waste Administration	477,224	426,098	89%	605,881	157,079	26%

- Solid Waste revenue is at 39% of budget and expenses are at 26% of budget for the year.

**Reclassification of Administrative Services Director**

As the City Council is aware both the Administrative Services Director (ASD) and Finance Manager resigned in January of this year. In response, staff acquired the services of Edie Bailey, LLP to provide interim financial services. As a result of the vacancies, staff conducted an assessment of the City’s Finance Division to determine if the current staffing levels and reporting structure are adequate to meet the needs of the City. The conclusion reached was that the overall number of staff in the Finance Division and the individual job specifications were sufficient, with the exception of the Administrative Services Director (ASD).

As defined, the ASD is responsible for overseeing the City’s Finance, Human Resources (HR), and Information Technology (IT) divisions. Each division has a manager that supervises the daily activities of the staff and reports to the director. In concept, this structure can function adequately depending on the size of the organization, the skill level of the staff in each division, and the percentage of administrative versus technical work that must be performed by the director. In larger organizations which may have numerous skilled positions in specific areas of expertise, the ASD can function as



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more of a true administrator and does not necessarily need to have experience in one or more of the subject areas under their responsibility. This becomes more challenging in smaller organizations where the director is more of a “working manager”. They will most likely have their own projects and tasks to accomplish, as well as a need to function as a subject expert to the staff, making it difficult for them to give the division managers the support they need.

In addition, given the high level of expectations that the City Council and community have regarding the quality and frequency of fiscal reporting and analysis, it would be judicious to have an experienced public sector financial expert overseeing the City’s financial services function on a fulltime basis. To accomplish this the Interim City Manager will be restructuring the division and replacing the ASD position with a Finance Director. This will allow the City to recruit an experienced professional with a strong public sector finance background. It will also emphasize the commitment of the City to vigorous financial management within the organization. Finally, it will provide the City with high level managerial oversight of the City’s finance activities on a daily basis.

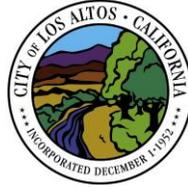
As to the IT and HR divisions, they will be placed under the supervision of the City Manager’s Office. These two divisions do not require the same level of day-to-day management oversight, nor have the same breadth of activities as Financial Services and so should function adequately in this new structure. Once the City’s new City Manager is on board, he or she can conduct their own assessment and determine if further adjustments need to be made.

It is important that the process for hiring a Finance Director begins now and does not wait for a new City Manager to come on board. It can take between four to six months to hire a qualified management professional, so the City cannot afford to wait until late in 2021 to fill this important position. However, while the recruitment will begin now, it can be left open until the new City Manager is announced and filled by new manager.

This restructuring will be cost neutral as the Finance Director will be at the same salary range as the ASD. Therefore, to implement this restructuring the following steps must be taken.

- Reclassification of the Administrative Services Director to Finance Director
- Updating Salary Schedule as part of mid-year budget item on March 23, 2021 to include Finance Director (same salary range as Admin Services Director)
- Securing services of firm to conduct recruitment for Finance Director, beginning after March 23<sup>rd</sup>.

### **Proposed Mid-year Budget Adjustments**



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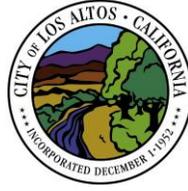
**Operating Budget:** The following are proposed adjustments are recommended for the General Fund. With the adjustments to both revenues and expenditures, the budget for FY 2020-21 is balanced.

**Revenues:**

General Fund Revenues	Approved FY 20-21 Budget	Proposed Adjustments	Revised FY 20-21 Budget
Property Tax	27,687,029	(400,000)	27,287,029
Sales Tax	2,641,120		2,641,120
Utility Users Tax	2,864,430	(400,000)	2,464,430
Transient Occupancy Tax	1,882,200	(1,300,000)	582,200
Business License Tax	468,180		468,180
Construction Tax	190,600		190,600
Documentary Transfer Tax	551,157		551,157
Interest Income	381,045		381,045
Rental Income	24,000		24,000
Recreation Fees	738,500	(700,000)	38,500
Community Development Fees	3,261,240	50,000	3,311,240
Franchise Fees	2,353,076		2,353,076
Administrative Fees	918,500		918,500
Police Fees	815,066		815,066
Miscellaneous Revenue	131,126		131,126
<b>Total General Fund Revenue</b>	<b>44,907,270</b>	<b>(2,750,000)</b>	<b>42,157,270</b>

- **Reduce Property Tax \$400,000**
- **Reduce Utility User Tax \$400,000**
- **Reduce Transient Occupancy Tax - \$1,300,000**
- **Reduce Recreation Fees - \$700,000**
- **Increase Community Development - Plan Checking Revenue (\$50K)** – An increase in Plan Checking revenues is requested so that it will offset the increase in expenditures as a result of the current level of development activity.

**Expenditures**



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To balance the budget, it is necessary to reduce General Fund Expenditures by \$1.4 million. Staff is confident that Expenditures can be reduced by this amount and is in the process of determining how much each department budget will be reduced by. Once this information is finalized, this section will be updated with those numbers.

- **Updated Salary Schedule (No fiscal impact)**  
An updated salary schedule for the current fiscal year is included as Attachment 2 in this report. The only change to the Salary Schedule is to add a new classification of Finance Director. Any costs are offset by current vacancy savings.

**Allocation of Unassigned Fund Balance (\$7.86M):**

Currently the City has \$7.86M in unassigned fund balance from the revenue over expenses achieved in FY 2019-20. Staff’s recommendation is to assign this amount to the City’s reserves as follows:

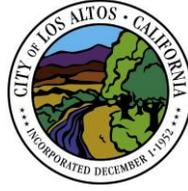
- Emergency and Operating Reserve – Add \$1.48 million to meet the 20% reserved per policy
- Add \$6.37 million to the Capital Improvement Projects (CIP) fund – to fund CIP costs for this year and future projects.

<b>Assigned Fund Balance</b>	<b>As of June 30, 2020</b>	<b>Proposed Allocation</b>	<b>Reserves after Allocation</b>
Emergency and Operating	\$ 7,206,207	\$ 1,487,400	\$ 8,693,607
OPEB	\$ 1,500,000		\$ 1,500,000
PERS Reserves	\$ 5,000,000		\$ 5,000,000
Technology Reserves	\$ 1,412,090		\$ 1,412,090
CIP Reserves	\$ 3,864,566	\$ 6,373,896	\$ 10,238,462
Community Center Reserve	\$ 10,654,976		\$ 10,654,976
Equipment Reserve	\$ 663,202		\$ 663,202
<b>Total Assigned Fund Balances</b>	<b>\$ 30,301,041</b>	<b>\$ 7,861,296</b>	<b>\$ 38,162,337</b>

**Capital Improvement Program**

The City’s Capital Improvement Program (CIP) consists of a multitude of projects at varying phases of the project cycle. The entire CIP plan will be reviewed and discussed in detail at a future City Council study session.

**Options**



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- 1) Adopt Resolution No. 2021-##, approving the mid-year report and proposed budget adjustments and updated salary schedule

**Advantages:** Adjustments made will ensure proper funding and spending within budgeted amounts. Reserves will be properly assigned

**Disadvantages:** None identified

- 2) Do not adopt Resolution No. 2021-## approving the mid-year report and proposed budget adjustments and updated salary schedule

**Advantages:** None identified

**Disadvantages:** Expenditures may not be properly aligned with current budget. Fund balances will remain unassigned

**Recommendation**

The staff recommends Option 1.